Consolidated Financial Statements

for the period ended 31 March 2008

Contents

Independent auditor's report 1

Group income statement 2

Group statement of recognised income and expense 2

Group balance sheet 3

Group cash flow statement 4

Notes to the Consolidated Financial Statements 5

Glossary of key terms 33

Independent auditor's report

to the general members meeting of Alliance Boots GmbH

As Group auditor, we have audited the accompanying Consolidated Financial Statements (Group income statement, Group statement of recognised income and expense, Group balance sheet, Group cash flow statement and related notes) of Alliance Boots GmbH for the period ended 31 March 2008.

Directors' responsibility

The Directors are responsible for the preparation of the Consolidated Financial Statements in accordance with International Financial Reporting Standards and the requirements of Swiss law. This responsibility includes designing, implementing and maintaining an internal control system relevant to the preparation of Consolidated Financial Statements that are free of material misstatement, whether due to fraud or error. The Directors are further responsible for selecting and applying appropriate accounting policies and making accounting estimates that are reasonable in the circumstances.

Auditor's responsibility

Our responsibility is to express an opinion on these Consolidated Financial Statements based on our audit. We conducted our audit in accordance with Swiss Auditing Standards and with the International Standards on Auditing (ISA). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Consolidated Financial Statements are free from material misstatement. We confirm that we meet the licensing and independence requirements as stipulated by Swiss law.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the Consolidated Financial Statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the Consolidated Financial Statements, whether due to fraud or error. In making those risk assessments, the auditor considers the internal control system relevant to the entity's preparation of the Consolidated Financial Statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control system. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made, as well as evaluating the overall presentation of the Consolidated Financial Statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the Consolidated Financial Statements give a true and fair view of the financial position of Alliance Boots GmbH and of its financial performance and its cash flows for the period then ended, in accordance with International Financial Reporting Standards and comply with Swiss law.

Reporting on other legal requirements

In accordance with article 728a paragraph 1 item 3 CO and Swiss Auditing Standard 890, we confirm that an internal control system relevant to the preparation of the Consolidated Financial Statements based on the criteria established by the Directors exists.

We recommend that the Consolidated Financial Statements submitted to you be approved.

KPMG Klynveld Peat Marwick Goerdeler SA

John A. Morris
Auditor in charge

Dr. Elisabeth Kruck

Zug, Switzerland
4 June 2008

Group income statement
for the period ended 31 March 2008

	Notes	£million
Revenue	4	**11,865**
Profit from operations before share of post tax earnings of associates and joint ventures	4, 5	**486**
Share of post tax earnings of associates and joint ventures	17	**49**
Profit from operations	7	**535**
Finance income	10	**254**
Finance costs	11	**(853)**
Loss before tax		**(64)**
Tax	12	**74**
Profit for the period		**10**
Attributable to:		
Equity shareholders of the Company		**10**
Minority interests		**–**
		10

All income and expense of the Group arose from continuing operations.

Group statement of recognised income and expense
for the period ended 31 March 2008

	£million
Exchange differences on translation of non-Sterling denominated operations	**101**
Defined benefit pension schemes – actuarial gains and losses	**181**
Gains deferred in hedging reserve	**1**
Available-for-sale investments – losses on revaluation deferred in equity	**(24)**
	259
Tax on items taken directly to equity	**(54)**
Income and expense recognised directly in equity	**205**
Profit for the period	**10**
Total recognised income and expense for the period	**215**
Attributable to:	
Equity shareholders of the Company	**213**
Minority interests	**2**
	215

Group balance sheet

as at 31 March 2008

	Notes	£million
Assets		
Non-current assets		
Goodwill	13	**4,514**
Other intangible assets	14	**5,460**
Property, plant and equipment	16	**2,078**
Investments in associates and joint ventures	17	**910**
Available-for-sale investments	18	**48**
Other receivables	20	**66**
Deferred tax assets	23	**66**
Retirement benefit assets	34	**317**
Derivative financial instruments	25	**1**
		13,460
Current assets		
Inventories	19	**1,422**
Trade and other receivables	20	**2,130**
Cash and cash equivalents	21	**413**
Restricted cash	22	**366**
Derivative financial instruments	25	**2**
		4,333
Total assets		17,793
Liabilities		
Current liabilities		
Borrowings	25	**(733)**
Trade and other payables	24	**(2,509)**
Current tax liabilities		**(30)**
Provisions	29	**(31)**
Derivative financial instruments	25	**(22)**
		(3,325)
Net current assets		1,008
Non-current liabilities		
Borrowings	25	**(8,585)**
Other payables	24	**(25)**
Deferred tax liabilities	23	**(1,545)**
Retirement benefit obligations	34	**(20)**
Provisions	29	**(57)**
Derivative financial instruments	25	**(188)**
		(10,420)
Net assets		4,048
Equity		
Share capital	30, 31	**1,005**
Share premium	30	**2,795**
Retained earnings	30	**137**
Other reserves	30	**76**
Shareholders' equity	30	4,013
Minority interests	30	35
Total equity	30	4,048

Group cash flow statement

for the period ended 31 March 2008

	Notes	£million
Operating activities		
Profit from operations		535
Adjustments to reconcile profit from operations to cash generated from operations:		
Share of post tax earnings of associates and joint ventures		(49)
Depreciation and amortisation		256
Decrease in inventories		34
Decrease in receivables		224
Decrease in payables and provisions		(265)
Movement in retirement benefit assets and obligations		(116)
Cash generated from operations		619
Tax paid		(58)
Net cash from operating activities		561
Investing activities		
Acquisition of businesses		(10,790)
Cash and cash equivalents of businesses acquired net of overdrafts		420
Disposal of businesses		20
Purchase of investments in associates and joint ventures		(41)
Purchase of available-for-sale investments		(3)
Purchase of property, plant and equipment, and intangible assets		(222)
Disposal of property, plant and equipment, and intangible assets		19
Dividends received from associates and joint ventures		19
Interest received		61
Net cash used in investing activities		(10,517)
Financing activities		
Interest paid		(598)
Interest element of finance lease obligations		(4)
Proceeds from borrowings		8,200
Repayment of borrowings		(621)
Fees associated with raising finance		(246)
Cash and cash equivalents transferred to restricted cash		(366)
Issue of ordinary share capital		3,800
Repayment of capital element of finance lease obligations		(16)
Contribution from minority interests		17
Net cash from financing activities		10,166
Net increase in cash and cash equivalents in the period		210
Cash and cash equivalents at beginning of period		–
Currency translation differences		(13)
Cash and cash equivalents at 31 March 2008	21	197

All cash flows of the Group arose from continuing operations.

Notes to the Consolidated Financial Statements
for the period ended 31 March 2008

1. General information
Alliance Boots GmbH is a private company incorporated in Switzerland. The address of its registered office is Alliance Boots GmbH, Baarerstrasse 78, CH-6300 Zug, Switzerland. The principal activities of the Group are pharmacy-led health & beauty retailing and pharmaceutical wholesaling in many major international markets.

2. Accounting policies
The principal accounting policies adopted in the preparation of the Consolidated Financial Statements are set out below:

Basis of accounting
The Consolidated Financial Statements are prepared in Sterling reflecting the denomination of the currency of the most significant proportion of the trade and cash flows of the Group and are rounded to the nearest £1 million. The Consolidated Financial Statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) as they apply to the Consolidated Financial Statements for the period ended 31 March 2008. Had the Consolidated Financial Statements been prepared under International Financial Reporting Standards as adopted by the European Union, there would be no material changes to the information presented in these Consolidated Financial Statements.

The Consolidated Financial Statements have been prepared on the historical cost basis, except for certain areas where fair value measurement required by a specific standard has been applied as identified in the accounting policies below.

The preparation of Consolidated Financial Statements in conformity with IFRSs requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts in the Consolidated Financial Statements. The areas involving a higher degree of judgement or complexity, or areas where assumptions or estimates are significant to the Consolidated Financial Statements are disclosed in note 36.

Alliance Boots GmbH was registered on 18 March 2008. On 31 March 2008 Alliance Boots GmbH acquired investments held by AB Acquisitions Holdings Limited in exchange for the issue of share capital, and became a subsidiary of that company.

On 26 June 2007 Alliance Boots plc was acquired by AB Acquisitions Limited, a company controlled by certain funds advised by Kohlberg Kravis Roberts & Co. L.P. and Stefano Pessina. Alliance Boots GmbH gained control of AB Acquisitions Limited on 31 March 2008, however the intermediate holding companies along with the ultimate parent company, AB Acquisitions Holdings Limited, have continued to be under the same common control. Under IFRS transactions involving companies under common control, including the acquisition of the intermediate parent companies by Alliance Boots GmbH, are accounted for at book value (rather than fair value), and the results for the Group are presented as if each of these transactions had taken place at the start of the earliest period presented.

The effect of this is that the Consolidated Financial Statements of Alliance Boots GmbH are presented for the period from 13 April 2007 (the earliest date of common control) to 31 March 2008, and include the results of the Alliance Boots plc group from the date of acquisition on 26 June 2007. The assets and liabilities of Alliance Boots plc have been consolidated at their fair value at the date of acquisition. The transactions leading to the introduction of Alliance Boots GmbH are accounted for at book value and no further fair valuation exercise is required in relation to the acquisition of Alliance Boots plc.

Standards, amendments and interpretations that are not yet effective and have not been adopted early by the Group
The following standards, amendments and interpretations have been published and are available for early adoption but have not yet been applied in these Consolidated Financial Statements:

- IFRS 8, Operating Segments: Effective for accounting periods commencing on or after 1 January 2009;
- IAS 1 (Amendment), Presentation of Financial Statements: Effective for accounting periods commencing on or after 1 January 2009;
- IAS 23 (Amendment), Borrowing Costs: Effective for accounting periods commencing on or after 1 January 2009;
- IAS 27 (Amendment), Consolidated and Separate Financial Statements: Effective for accounting periods commencing on or after 1 July 2009;
- IAS 32 and IAS 1 (Amendments), Puttable Financial Instruments and Obligations Arising on Liquidation: Effective for accounting periods commencing on or after 1 January 2009;
- IFRS 2 (Amendment), Share Based Payment – Vesting Conditions and Cancellations: Effective for accounting periods commencing on or after 1 January 2009;
- IFRS 3 (Amendment), Business Combinations: Effective for accounting periods commencing on or after 1 July 2009;
- IFRIC 12, Service Concession Arrangements: Effective for accounting periods commencing on or after 1 June 2008;
- IFRIC 13, Customer Loyalty Programmes: Effective for accounting periods commencing on or after 1 July 2008; and
- IFRIC 14, IAS 19, The Limit on a Defined Benefit Asset, Minimum Funding Requirements and Their Interaction: Effective for accounting periods commencing on or after 1 January 2008.

The Directors do not anticipate that the adoption of these standards will have a material impact on the Consolidated Financial Statements in the period of initial application with the exception of the amendment to IFRS 3 and IFRIC 14 where it is not possible to estimate the impact in the period of initial application as their impact is dependent on future events.

2. Accounting policies (continued)

Consolidation

The Consolidated Financial Statements as at and for the period ended 31 March 2008 comprise the Company and its subsidiaries and their interests in associates and joint ventures (together referred to as the "Group").

Subsidiaries are entities over which the Group has the power to govern the financial and operating policies so as to obtain benefits from their activities. The results of subsidiaries acquired or disposed of during the period are included in the Group income statement from and to the date that control commences or ceases, as appropriate.

An associate is an entity over which the Group, either directly or indirectly, is in a position to exercise significant influence by participating in, but without control, or joint control, of the financial and operating policies of the entity.

A joint venture is an entity over which the Group, either directly or indirectly, is in a position to jointly control the financial and operating policies of the entity.

Associates and joint ventures are accounted for using the equity method. Unrealised profits and losses recognised by the Group on transactions with associates or joint ventures are eliminated to the extent of the Group's interest in the associate or joint venture concerned. Financial statements of some associates and joint ventures are prepared for different reporting periods from that of the Group. Adjustments are made for the effects of transactions and events that occur between the reporting date of an associate or joint venture and reporting the Consolidated Financial Statements.

All intra-group transactions, balances and unrealised gains on transactions between Group companies are eliminated on consolidation.

Currency

Currency transactions

At entity level, transactions in currencies other than the entity's functional currency are translated into the entity's functional currency at the exchange rate ruling at the date of the transactions. Monetary assets and liabilities denominated in non-Sterling denominated currencies at the balance sheet date are translated at the exchange rate ruling at that date. Non-monetary assets and liabilities that are measured in terms of historical cost in non-Sterling denominated currencies are translated using the exchange rates at the date of the transaction. Non-monetary items measured at fair value in a non-Sterling denominated currency are translated using the exchange rates at the date when the fair value was determined. Exchange gains and losses are recognised in the income statement.

Non-Sterling denominated operations

The assets and liabilities of non-Sterling denominated operations, including goodwill and fair value adjustments arising on consolidation, are translated into Sterling at exchange rates ruling at the balance sheet date. The results and cash flows of non-Sterling denominated subsidiaries are translated into Sterling at the average exchange rate for the period, which approximates to the underlying actual rates.

Exchange differences arising from the translation of the results and net assets of non-Sterling denominated subsidiaries are recognised in the translation reserve.

When a non-Sterling denominated operation is sold, the related balance in the translation reserve is recognised in the income statement as part of the gain or loss on sale.

Revenue

Revenue shown on the face of the income statement is the amount derived from the sale of goods and services in the normal course of business outside of the Group, net of trade discounts, value added tax and other sales-related taxes. Revenue from the sale of goods is recognised when the Group has transferred the significant risks and rewards of ownership and control of the goods sold and the amount of revenue can be measured reliably. Revenue from services is recognised when it is probable that the economic benefits associated with the transaction will flow to the entity and the amount of revenue can be measured reliably.

The accounting policies for the major revenue categories by business segment are as follows:

Health & Beauty Division

Reimbursement of dispensing revenue is initially estimated because the actual reimbursement is often not known until after the month of sale.

Consideration received from retail sales is recorded as revenue when the Group has completed full performance in respect of that consideration, which is at the point of sale.

In respect of loyalty schemes (principally the Boots Advantage Card), as points are issued to customers, the retail value of those points expected to be redeemed is deferred. When the points are used by customers they are recorded as revenue. Sales of gift vouchers are only included in revenue when vouchers are redeemed.

Pharmaceutical Wholesale Division

Wholesale revenue is recognised upon despatch of goods.

When the Group acts in the capacity of an agent, or a logistic service provider, revenue is the service fees and is recognised upon performance of the services concerned.

Contract Manufacturing

Revenue is recognised upon despatch of goods.

Supplier rebates
Certain suppliers offer rebates when purchases made in a period meet or exceed a predetermined level. Rebates are only recognised when there is clear evidence of this type of binding arrangement with the supplier and the rebate receipt is both probable and can be reasonably estimated. The rebate is recognised as a reduction in the purchase price.

Exceptional items
Exceptional items are items classified by Alliance Boots GmbH as exceptional in nature. These are not regarded as forming part of the trading activities of the Group and so merit separate presentation to allow stakeholders to understand the elements of financial performance and to assess the trends in financial performance.

Finance income
Finance income comprises interest receivable on funds invested calculated using the effective interest rate method, exchange gains, expected returns on pension scheme assets, gains on hedging instruments that are recognised in the income statement and dividends received from investments.

Finance costs
Finance costs comprise interest payable on borrowings calculated using the effective interest rate method, financing fees, exchange losses, interest on pension scheme liabilities, the interest expense component of finance lease payments and losses on hedging instruments that are recognised in the income statement.

Current/non-current classification
Current assets include assets held primarily for trading purposes, cash and cash equivalents, restricted cash and assets expected to be realised in, or intended for sale or consumption in, the course of the Group's operating cycle. All other assets are classified as non-current assets.

Current liabilities include liabilities held primarily for trading purposes, liabilities expected to be settled in the course of the Group's operating cycle and those liabilities due within one year from the reporting date. All other liabilities are classified as non-current liabilities.

Business combinations and goodwill
Business combinations are accounted for under IFRS 3 using the purchase method of accounting. The cost of acquisition is the consideration given in exchange for the identifiable net assets. This consideration includes any cash paid plus the fair value at the date of exchange of assets given, liabilities incurred or assumed and equity instruments issued by the Group. The cost of acquisition also includes directly attributable costs.

The acquired net assets are initially recognised at fair value (which is deemed cost in the Consolidated Financial Statements). Where the Group does not acquire 100% ownership of the acquired company, a minority interest is recorded as the minority's proportion of the fair value of the acquired net assets. Any adjustment to the fair values is recognised within twelve months of the acquisition date.

Goodwill on acquisitions comprises the excess of the fair value of the consideration plus any directly attributable costs over the fair value of the identifiable net assets acquired. Any goodwill and fair value adjustments are recorded as assets and liabilities of the acquired business and are recorded in the local currency of that business. The costs of integrating and reorganising acquired businesses are charged to the post-acquisition income statement.

Goodwill is carried at cost less accumulated impairment losses. No amortisation is charged.

Intangible assets
Intangible assets are stated at cost or deemed cost less any impairment and accumulated amortisation. The principal categories of intangible assets are:

Pharmacy licences
Pharmacy licences, being the exclusive right to operate as a pharmacy, are capitalised where there is an asset that can be separated from other identifiable assets that together form a pharmacy business.

Brands
Brands consist of corporate and product brands acquired as part of business combinations that meet the criteria for separate recognition. Costs in relation to internally generated brands are not capitalised.

Customer relationships
Customer relationships consist of relationships with customers established through contracts or non-contractual customer relationships that meet the criteria for separate recognition, that have been acquired in a business combination.

Product licences
Licences which give the right to sell certain products in specific countries are recognised separately as an intangible asset when they are acquired.

Software
Software that is not integral to an item of property, plant and equipment is recognised separately as an intangible asset. Certain direct and indirect development costs associated with internally developed software, including direct costs of materials and services, and payroll costs for employees devoting time to the software projects, are capitalised once the project has reached the application development stage. The costs are amortised from when the asset is ready for use. Costs incurred during the preliminary project stage, maintenance and training costs, and research and development costs are expensed as incurred.

2. Accounting policies (continued)

Amortisation

Where an intangible asset is considered to have a finite life, amortisation is charged to the income statement on a straight-line basis over the useful life from the date the asset is available for use. Pharmacy licences recognised as intangible assets do not expire and therefore are considered to have an indefinite life. Certain brands have been identified as having an indefinite life, based on their life and history along with current market strength and future development plans. Those assets considered to have an indefinite life are not amortised and are tested for impairment at each balance sheet date. The useful lives for those intangible assets with a finite life are as follows:

- Brands – 10 to 20 years;
- Customer relationships – 4 to 20 years;
- Product licences – 5 to 15 years; and
- Software – 3 to 8 years.

Amortisation periods and methods are reviewed annually and adjusted if appropriate.

Property, plant and equipment

All property, plant and equipment is stated at cost or deemed cost less accumulated depreciation and impairment losses.

Depreciation of property, plant and equipment is provided to write off the cost, less residual value, in equal instalments over their expected useful economic lives as follows:

- Freehold land and assets in the course of construction – not depreciated;
- Freehold and long leasehold buildings – depreciated to their estimated residual values over their useful economic lives of not more than 50 years;
- Short leasehold properties – remaining period of lease;
- Plant and machinery – 3 to 10 years; and
- Fixtures, fittings, tools and equipment – 3 to 20 years.

Residual values, remaining useful economic lives and depreciation methods are reviewed annually and adjusted if appropriate.

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the income statement.

Impairment of assets

The Group's assets are reviewed at each balance sheet date to determine whether events or changes in circumstances exist that indicate that their carrying amount may not be recoverable. If such an indication exists, the asset's recoverable amount is estimated. The recoverable amount is the higher of an asset's fair value less costs to sell and its value in use. An impairment loss is recognised in the income statement for the amount by which the asset's carrying amount exceeds its recoverable amount. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (referred to as cash generating units).

For goodwill and other intangible assets that have an indefinite life and assets not yet available for use, the recoverable amount is estimated annually or more frequently when there is an indication that the asset is impaired.

Non-current assets held for sale and discontinued operations

Non-current assets and disposal groups are classified as held for sale if their carrying amount will be recovered through sale rather than through continuing use. The asset or disposal group must be available for immediate sale and the sale must be highly probable and be expected to complete within one year of the balance sheet date. Where applicable, non-current assets and disposal groups classified as held for sale are measured at the lower of fair value less costs to sell and carrying amount.

Impairment losses on initial classification as held for sale are included in the income statement. Gains reversing previous impairment losses or losses on subsequent remeasurements are also included in the income statement.

Assets classified as held for sale are disclosed separately on the face of the balance sheet and classified as current assets or liabilities with disposal groups being separated between assets held for sale and liabilities held for sale. No amortisation or depreciation is charged on non-current assets (including those in disposal groups) classified as held for sale.

A discontinued operation is a component of the Group's business that represents a separate major line of business or geographical area of operations that has been disposed of, has been abandoned or meets the criteria for classification as held for sale. Where applicable, discontinued operations are presented in the income statement as a separate line entitled 'Profit after tax from discontinued operations'.

Available-for-sale investments

The Group classifies its listed and unlisted investments as available-for-sale financial assets and measures them at fair value. The fair values of quoted investments are based on current bid prices and for investments where there is no quoted market price, fair value is determined by using valuation techniques, such as estimated discounted cash flows or by reference to the current market value of similar investments. Gains and losses arising from changes in fair values and exchange translation are recognised in equity until the investment is either disposed or derecognised. When an investment is disposed or derecognised, the related balance in the available-for-sale reserve is recognised in the income statement as part of the gain or loss on sale.

Inventories
Inventories are valued at the lower of cost and net realisable value. With the exception of retail inventory in the Health & Beauty Division, cost is determined using the first in, first out (FIFO) method. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs necessary to make the sale.

The cost of raw materials and packaging is their purchase price. The cost of work in progress and finished goods comprises the purchase cost of goods, direct labour and those overheads related to manufacture and distribution based on normal activity levels. Retailing merchandise is valued at retail prices and reduced by appropriate margins to take into account factors such as average cost, obsolescence, seasonality and damage.

Cash and cash equivalents
Cash and cash equivalents comprises cash in hand and short term deposits with maturities of three months or less from the date of acquisition. Bank overdrafts are shown within borrowings in current liabilities on the balance sheet. Bank overdrafts are included as a component of cash and cash equivalents for the purpose of the cash flow statement.

Restricted cash
Restricted cash comprises deposits, the use of which is restricted for specific purposes and so is not available for the use of the Group in its day-to-day operations.

Financial instruments and derivative financial instruments
Financial assets and liabilities are recognised in the balance sheet at fair value when the Group becomes a party to the contractual provisions of the instrument. The Group uses derivative financial instruments to hedge its exposure to currency translation and interest rate risks arising from operating, financing and investing activities.

In accordance with its treasury policy, the Group does not hold or issue derivative financial instruments for trading purposes. However, derivatives that do not qualify for hedge accounting are accounted for at fair value with movements taken to the income statement.

Derivative financial instruments are recognised initially at fair value, with movements on remeasurement recognised immediately in the income statement. However, where derivatives qualify for hedge accounting, recognition of any resultant gain or loss depends on the nature of the item being hedged (see below).

The fair value of interest rate swaps is the estimated amount that the Group would receive or pay to terminate the swap at the balance sheet date, taking into account current interest rates and the current creditworthiness of the swap counterparties.

The fair value of forward exchange contracts is their market price at the balance sheet date.

Hedges
Cash flow hedges
Where a derivative financial instrument is designated as a hedge of the variability in cash flows of a recognised asset or liability, or a highly probable forecasted transaction, the effective part of any gain or loss on the derivative financial instrument is recognised directly in the hedging reserve.

When the forecasted transaction subsequently results in the recognition of a non-financial asset or non-financial liability the associated cumulative gain or loss is removed from equity and included in the initial cost or other carrying amount of the non-financial asset or liability.

If the hedged forecasted transaction subsequently results in the recognition of a financial asset or financial liability, the associated gains and losses that were recognised directly in equity are reclassified into profit or loss in the same period, or periods, during which the asset acquired or liability assumed affects profit or loss.

For cash flow hedges, other than those covered by the preceding two policy statements, the associated cumulative gain or loss is removed from equity and recognised in the income statement in the same period, or periods, during which the hedged forecast transaction affects profit or loss. The ineffective part of any gain or loss is recognised immediately in the income statement.

When a hedging instrument expires or is sold, terminated or exercised, or the entity revokes designation of the hedge relationship but the hedged forecast transaction is still expected to occur, the cumulative gain or loss at that point remains in equity and is recognised in accordance with the above policy when the transaction occurs. If the hedged transaction is no longer expected to take place, the cumulative unrealised gain or loss recognised in equity is recognised immediately in the income statement.

Fair value hedges
Where a derivative financial instrument hedges the changes in the fair value of a recognised asset or liability or an unrecognised firm commitment (or an identified portion of such an asset, liability or firm commitment), any gain or loss on the hedging instrument is recognised in the income statement. The hedged item is also stated at fair value in respect of the risk(s) being hedged, with any gain or loss recognised in the income statement.

Hedge of monetary assets and liabilities
Where a derivative financial instrument is used to hedge economically the currency translation exposure of a recognised monetary asset or liability, no hedge accounting is applied and any gain or loss on the hedging instrument is recognised in the income statement.

Hedge of net investment in non-Sterling denominated operations
On consolidation, the effective portion of the gain or loss on an instrument designated as a hedge of net investment in a non-Sterling denominated operation that is determined to be an effective hedge is recognised directly in the translation reserve. The ineffective portion is recognised immediately in the income statement.

2. Accounting policies (continued)

Borrowings

Borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, borrowings are stated at amortised cost with any difference between cost and redemption value being recognised in the income statement over the period of the borrowings on an effective interest basis.

Employee benefits

Pensions

The Group operates a number of pension schemes under which contributions by employees and by the sponsoring companies are held in trust funds separated from the Group's finances. Where a pension arrangement is unfunded, provision is made in the balance sheet for the obligation.

Defined benefit schemes:
A defined benefit scheme is a pension scheme that defines an amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors, such as age, years of service and compensation. The Group's net obligation or asset in respect of defined benefit pension schemes is calculated separately for each scheme by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine its present value and the fair value of any scheme assets is deducted.

The discount rate is the yield at the balance sheet date on AA rated bonds that have maturity dates approximating to the terms of the Group's obligations. The calculation is performed by a qualified actuary using the projected unit credit method. Scheme assets are valued at bid price.

Current and past service costs are recognised in profit from operations, finance costs include interest on pension scheme liabilities and the expected return on scheme assets is included in finance income. Past service costs are recognised immediately to the extent that the benefits are already vested, otherwise they are amortised on a straight-line basis over the average period until the benefits become vested. All actuarial gains and losses that arise in calculating the Group's obligation in respect of a scheme are recognised immediately in reserves and reported in the statement of recognised income and expense.

Defined contribution schemes:
Obligations for contributions to defined contribution pension schemes are recognised as an expense in the income statement as they fall due.

Leases

Leases, for which the Group assumes substantially all the risks and rewards of ownership, are classified as finance leases, including outsourced assets held exclusively for the use of the Group. The cost of assets held under finance leases is included within property, plant and equipment and depreciation is provided in accordance with the policy for the class of asset concerned over the length of the lease. The corresponding obligations under these leases are shown as liabilities. The finance charge element of rentals is charged to the income statement through finance costs to produce, or approximate to, a constant periodic rate of charge on the remaining balance of the outstanding obligations. Lease premiums paid are treated as prepayments and are amortised over the period of the lease.

Payments made under operating leases are recognised in the income statement on a straight-line basis over the term of the lease. Predetermined rental increases included in the lease are recognised on a straight-line basis. Benefits received as an incentive to sign a lease, whatever form they may take, are credited to the income statement on a straight-line basis over the lease term.

Taxation

Tax on the profit or loss for the period represents the sum of the tax currently payable and deferred tax. Tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current taxation

Current tax is the expected tax payable on the taxable profit for the period. Taxable profit differs from net profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates enacted or substantively enacted at the balance sheet date, and any adjustments to tax payable in respect of previous years.

Deferred taxation

Deferred tax is provided in full using the balance sheet liability method. It is the tax expected to be payable or recoverable on the temporary differences between the carrying amounts of assets and liabilities in the Consolidated Financial Statements and the corresponding tax bases used in the computation of taxable profit. The following temporary differences are not provided for: those arising from the initial recognition of goodwill, the initial recognition of assets and liabilities that affect neither accounting nor taxable profit and differences relating to investments in subsidiaries to the extent that it is not probable that they will reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. The carrying amounts of deferred tax assets are reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the asset to be recovered.

Additional income taxes that arise from receipt of dividends from the Group's subsidiary and associate and joint venture interests are recognised at the same time as the payee recognises the liability to pay the related dividend except where the timing of the payment is not controlled by the Group, in which case a deferred tax liability is recognised in full against those distributable reserves.

Deferred tax assets and liabilities are offset in the balance sheet when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

Provisions

Provisions are recognised in the balance sheet when there is a present legal or constructive obligation as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and that obligation can be measured reliably. If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects the risks specific to the liability.

3. Exchange rates

The significant exchange rates relative to Sterling used in the preparation of the Consolidated Financial Statements were as follows:

	Average post acquisition of Alliance Boots plc	At 31 March 2008
Euro	1.402	1.272
Turkish Lira	2.474	2.566
Swiss Franc	2.298	1.995

4. Segmental information

Segmental information is presented in respect of the Group's business and geographical segments. The primary format (business segments) is based on the Group's management and internal reporting structure. Inter-segment pricing is determined on an arm's length basis.

The Group comprises the following business segments:

Health & Beauty Division

Comprises all the pharmacy-led health and beauty retail businesses across the Group. These are in the UK, Norway, Republic of Ireland, The Netherlands, Thailand, Italy and Russia.

Pharmaceutical Wholesale Division

Comprises all the pharmaceutical wholesaling businesses across the Group. These are in France, UK, Spain, Italy, The Netherlands, Czech Republic, Russia and Norway.

Contract Manufacturing & Corporate Costs

Comprises activities which fall outside the Group's two Divisions being Contract Manufacturing and Corporate, including unrealised profit in stock adjustments. The profit contribution for Contract Manufacturing was allocated to the Health & Beauty Division.

Revenue and profit for the primary segments were as follows:

	Healthy & Beauty Division £million	Pharmaceutical Wholesale Division £million	Contract Manufacturing & Corporate Costs £million	Eliminations £million	Total £million
External revenue	5,323	6,461	81	–	11,865
Inter-segment sales	14	951	–	(965)	–
Total revenue	5,337	7,412	81	(965)	11,865
Trading profit/(loss)	468	159	(28)	–	599
Exceptional items (note 6)	(27)	(1)	(30)	–	(58)
Amortisation of customer relationships and brands	(26)	(29)	–	–	(55)
Profit from operations before share of post tax earnings of associates and joint ventures	415	129	(58)	–	486
Share of post tax earnings of associates and joint ventures					49
Profit from operations					535
Finance income					254
Finance costs					(853)
Loss before tax					(64)
Tax					74
Profit for the period					10

4. Segmental information (continued)

The primary segment assets and liabilities at 31 March 2008 were as follows:

	Assets £million	Liabilities £million	Total £million
Health & Beauty Division	10,804	(1,095)	9,709
Pharmaceutical Wholesale Division	4,980	(1,693)	3,287
Contract Manufacturing & Corporate	136	(84)	52
Eliminations	(250)	250	–
Net operating assets	15,670	(2,622)	13,048
Investments in associates and joint ventures			910
Available-for-sale investments			48
Current and deferred tax			(1,509)
Net borrowings			(8,746)
Net retirement benefit assets			297
Total			4,048

Eliminations include inter-segmental trading accounts between subsidiary companies.

Other segmental information in respect of the primary segments for the period ended 31 March 2008 was as follows:

	Health & Beauty Division £million	Pharmaceutical Wholesale Division £million	Contract Manufacturing & Corporate Costs £million	Total £million
Amortisation of other intangible assets	66	32	–	98
Depreciation of property, plant and equipment	129	23	6	158
Capital expenditure				
– other intangible assets	30	19	–	49
– property, plant and equipment	164	29	6	199

Geographical segments

Segment revenue is based on the geographical location of the customers. Segment assets are based on the geographical location of the assets. The secondary segment financial information for the period ended and at 31 March 2008 was as follows:

	Revenue £million	Capital expenditure £million	Segmental assets £million
UK	5,788	206	13,150
France	3,043	10	1,513
Other	3,112	32	3,185
Intra-group	(78)	–	(55)
	11,865	248	17,793

5. Profit from operations before share of post tax earnings of associates and joint ventures

	Before exceptional items and amortisation of customer relationships and brands £million	Exceptional items £million	Amortisation of customer relationships and brands £million	Total £million
Revenue	11,865	–	–	11,865
Cost of sales	(8,909)	–	–	(8,909)
Gross profit	2,956	–	–	2,956
Selling, distribution and store costs	(1,980)	(31)	(55)	(2,066)
Administrative costs	(377)	(27)	–	(404)
Profit/(loss) from operations before share of post tax earnings of associates and joint ventures	599	(58)	(55)	486

6. Exceptional items

	£million
Costs in relation to merger cost synergies	8
Costs in relation to second phase of integration projects	17
Systems rationalisation and supply chain reconfiguration costs[1]	6
Costs in relation to the acquisition of Alliance Boots plc	27
	58

[1] Associated with the systems rationalisation and supply chain reconfiguration programme in the UK business within the Health & Beauty Division.

7. Profit from operations

The following items have been deducted in arriving at profit from operations:

	Notes	£million
Amortisation of other intangible assets		98
Depreciation of property, plant and equipment		
– owned assets		141
– held under finance leases		17
Research and development costs		1
Employee costs	9	1,495

An analysis of the total remuneration paid to the Group's principal auditor is provided below:

	£million
Audit of the Consolidated Financial Statements	0.8
Audit of subsidiary financial statements	1.9
Other services supplied as required by legislation	0.7
Other services relating to taxation	0.3
All other services	0.1

8. Acquisitions and disposals of businesses

Acquisitions

Alliance Boots plc

On 26 June 2007 the Group acquired 100% of the ordinary shares of Alliance Boots plc. The total purchase consideration of £11,059 million comprised £10,608 million cash and £366 million loan notes along with £85 million of costs incurred on the acquisition. The cash element of the consideration is shown net of £82 million in respect of proceeds from excess shares held in employee benefit trusts and £18 million of cash proceeds received on issue of shares to satisfy share options exercised on acquisition.

The core businesses of the acquired group are pharmacy-led health and beauty retailing and pharmaceutical wholesaling.

The book values of the identifiable assets and liabilities and their fair value to the Group at the date of acquisition were as follows:

	Book value before acquisition £million	Fair value adjustments £million	Fair value £million
Other intangible assets	1,516	3,841	5,357
Property, plant and equipment	1,671	336	2,007
Investments in associates and joint ventures	634	103	737
Available-for-sale investments	63	–	63
Net retirement benefit obligations	(3)	–	(3)
Inventories	1,359	–	1,359
Trade and other receivables	2,236	–	2,236
Net borrowings	(818)	(9)	(827)
Trade and other payables, and provisions	(2,605)	(75)	(2,680)
Current and deferred tax liabilities	(531)	(1,008)	(1,539)
	3,522	3,188	6,710
Minority interests			(16)
Goodwill arising on acquisition			4,365
			11,059
Satisfied by:			
Cash			10,608
Loan notes			366
Costs incurred on the acquisition			85
			11,059

From the date of acquisition, the acquired group contributed £603 million of trading profit to the Group.

The goodwill of £4,365 million represents the intangible assets that could not be individually separated and reliably measured due to their nature. This includes the view that the long term potential growth of Alliance Boots can best be achieved under private ownership and that, through experience of operating comparable business models and access to significant capital resources, the Group is well positioned for its next phase of development as a global leader in the healthcare services and beauty industries.

Other acquisitions

Other acquisitions during the period related to UK pharmacies purchased for a total consideration of £97 million.

8. Acquisitions and disposals of businesses (continued)

Disposals

During the period the Group disposed of pharmacies in accordance with the undertakings given to the Office of Fair Trading and also disposed of its prewholesale and contracts logistics business in Portugal to Alliance Healthcare S.A., the Group's Portuguese associate.

9. Employee costs

The average monthly number of persons employed by the Group over the period since the acquisition of Alliance Boots plc, including Directors and part-time employees, was:

	Number of heads	Full time equivalents
Health & Beauty Division	76,106	46,565
Pharmaceutical Wholesale Division	15,732	14,225
Contract Manufacturing & Corporate	1,272	1,242
	93,110	62,032

Costs incurred in respect of these employees were:

	£million
Wages and salaries	1,301
Social security costs	139
Pension costs	55
	1,495

10. Finance income

	£million
Bank deposit interest income	63
Gains on derivative financial instruments	23
Expected return on pension scheme assets	163
Other finance income	5
	254

11. Finance costs

	£million
Interest on bank loans and overdrafts[1]	567
Interest on loan notes	44
Interest on other loans	34
Financing fees[2]	46
Finance charges on finance leases	4
Interest on pension scheme liabilities	157
Other finance costs	1
	853

[1] Interest on bank loans and overdrafts includes £19 million of rolled up interest on mezzanine debt which is payable when the debt itself is repaid.
[2] Financing fees include £27 million of fees which are being amortised over the term of the financing being provided.

12. Tax

An analysis of the tax credit in the period was as follows:

	£million
Current tax	
Current tax for the period	(4)
Adjustments in respect of prior years	7
Current tax credit	3
Deferred tax	
Deferred tax relating to the origination and reversal of temporary differences	(19)
Adjustments due to changes in tax rates	90
Deferred tax credit	71
Tax credit in the income statement	74

The underlying tax charge, calculated before exceptional items, amortisation of customer relationships and brands, and other exceptional tax credits, reconciles to the tax credit in the period as follows:

	£million
Underlying tax charge	(55)
Tax on	
– exceptional items	22
– amortisation of customer relationships and brands	17
Other exceptional credits	90
	74

The Group's principal operations are in Europe and therefore the appropriate standard rate of tax is the average of the standard tax rates in the countries of operation, weighted by the amount of profit on ordinary activities before taxation. The reconciliation of expected total tax charge is based on this standard tax rate of 34.5%.

The tax rate, which we define as the tax credit expressed as a percentage of profit from operations before share of post tax earnings of associates and joint ventures, net of finance income and finance costs, was 65.5%.

In the current period the effective tax rate is lower than the expected rate of 34.5%, mainly as a result of the release of a net deferred tax liability of £90 million to reflect the reduction in the UK corporation tax rate from 30% to 28%, partially offset by the unrelieved losses arising in the period.

The reconciliation of the expected total tax charge was as follows:

	£million
Loss before tax	(64)
Less: share of post tax earnings of associates and joint ventures	(49)
	(113)
Expected tax credit at standard tax rate	39
Factors affecting credit for the period:	
Non-taxable/non-deductible items	(1)
Other differences	(6)
Deferred tax on unremitted earnings of associates and joint ventures	(4)
Unrelieved tax losses arising in the period	(52)
Deferred tax adjustments in respect of prior years	1
Current tax adjustments in respect of prior years	7
Rate change impact on deferred tax	90
Total tax credit	74

Tax on items taken directly to equity comprised:

	£million
Tax charge on defined benefit pension schemes – actuarial gains and losses	56
Tax credit on other temporary differences	(2)
	54

13. Goodwill

	£million
Cost and net book value	
At beginning of period	–
Acquisition of Alliance Boots plc	4,365
Other acquisitions	11
Currency translation differences	138
At 31 March 2008	4,514

14. Other intangible assets

	Pharmacy licences £million	Brands £million	Customer relationships £million	Product licences £million	Software £million	Total £million
Cost						
At beginning of period	–	–	–	–	–	–
Acquisition of Alliance Boots plc	1,162	2,979	1,101	3	112	5,357
Other acquisitions	96	–	–	–	–	96
Additions	–	–	–	–	49	49
Currency translation differences	2	–	53	–	6	61
At 31 March 2008	1,260	2,979	1,154	3	167	5,563
Amortisation						
At beginning of period	–	–	–	–	–	–
Charge for the period	–	3	52	–	43	98
Currency translation differences	–	–	3	–	2	5
At 31 March 2008	–	3	55	–	45	103
Net book value						
At 31 March 2008	1,260	2,976	1,099	3	122	5,460

15. Impairment testing of goodwill and other intangible fixed assets with indefinite lives

Goodwill, pharmacy licences and brands with indefinite useful lives are allocated to the appropriate cash generating units (CGUs) identified according to the country of operation and business. Those with significant amounts allocated at 31 March 2008 are shown in the table below:

	Goodwill £million	Pharmacy licences £million	Brands £million
Health & Beauty Division – UK	2,545	1,252	2,911
Pharmaceutical Wholesale Division – UK	1,034	–	–
Other	935	8	–
	4,514	1,260	2,911

Goodwill, pharmacy licences and brands with indefinite useful lives are subject to annual impairment testing, or more frequently if there are indications of impairment. The recoverable amounts of the CGUs are determined from value-in-use calculations which use discounted post tax cash flows from approved budgets and three year forecasts and extrapolated cash flows for the periods beyond these using estimated long term growth rates. The key assumptions are as follows:

- **Long term average growth rates** are used to extrapolate cash flows. These are determined with reference to both internal approved budgets and forecasts and available external long term growth data for both the country and business of each CGU's operation.
- **Discount rates** are calculated separately for each CGU and reflect the individual nature and specific risks relating to the business and the market in which it operates. These have been calculated using a weighted average cost of capital approach.
- **Gross margins** used are determined based on past performance and management's expectations of market development. No improvement to margins beyond periods covered by approved budgets and forecasts has been assumed.

The pre-tax discount rates used in the impairment tests at 31 March 2008 for each of the CGUs above were as follows:

	Discount rate %
Health & Beauty Division – UK	15.0
Pharmaceutical Wholesale Division – UK	15.0

The long term growth rate used in the impairment tests at 31 March 2008 was 4.4% for the UK businesses in the Health & Beauty and Pharmaceutical Wholesale Divisions.

16. Property, plant and equipment

	Land and buildings £million	Plant and machinery £million	Fixtures, fittings, tools and equipment £million	Total £million
Cost				
At beginning of period	–	–	–	–
Acquisition of Alliance Boots plc	1,069	111	827	2,007
Other acquisitions	1	–	1	2
Additions	19	34	146	199
Disposals	(19)	–	–	(19)
Business disposals	(1)	–	(1)	(2)
Currency translation differences	33	2	17	52
At 31 March 2008	1,102	147	990	2,239
Depreciation				
At beginning of period	–	–	–	–
Charge for the period	14	19	125	158
Currency translation differences	–	–	3	3
At 31 March 2008	14	19	128	161
Net book value				
At 31 March 2008	1,088	128	862	2,078

Included within the net book values above are amounts in respect of assets held under finance leases of £39 million in land and buildings, £9 million in plant and machinery and £33 million in fixtures, fittings, tools and equipment.

Property, plant and equipment includes payments on account and assets in the course of construction of £15 million.

17. Investments in associates and joint ventures

	£million
At beginning of period	–
Acquisition of Alliance Boots plc	737
Additions	41
Share of post tax earnings	49
Dividends	(19)
Currency translation differences	102
At 31 March 2008	910

Additions during the period related to the investment in a joint venture called Guangzhou Pharmaceuticals Corporation, a Chinese pharmaceutical wholesaler.

Details of the Group's principal associates and joint ventures are provided in note 35.

Included within the total carrying value of investments in associates and joint ventures was £444 million in respect of listed companies. Their market value, based on the closing share prices at 31 March 2008, was £368 million.

The aggregated assets and liabilities reported by associates and joint ventures at 31 March 2008 were as follows:

	£million
Total assets	3,160
Total liabilities	(2,143)
Net assets	1,017
Group share	377

The aggregated revenues reported by associates and joint ventures for the period ended 31 March 2008 were as follows:

	£million
Total revenue	5,201
Group share	1,904

The aggregated post tax earnings reported by associates and joint ventures for the period ended 31 March 2008 were as follows:

	£million
Total post tax earnings	121
Group share	49

18. Available-for-sale investments

	£million
At beginning of period	–
Acquisition of Alliance Boots plc	63
Additions	3
Movement in fair value	(24)
Currency translation differences	6
At 31 March 2008	**48**

Available-for-sale investments at 31 March 2008 comprised the following:

	£million
Listed securities	
– equity	38
– non-equity	9
Unlisted securities – equity	1

19. Inventories

	£million
Raw materials	32
Work in progress	11
Finished goods	1,379
	1,422

Included in the above are £30 million of inventories held at net realisable value. During the period, the write-down of inventories to net realisable value recognised as an expense in the income statement amounted to £16 million.

20. Trade and other receivables

	£million
Non-current	
Loans to customers	34
Other receivables	32
	66
Current	
Trade receivables	1,780
Loans to customers	81
Prepayments and accrued income	132
Other receivables	137
	2,130

All amounts within current trade and other receivables are due within one year.

21. Cash and cash equivalents

	£million
Bank balances	173
Short term deposits	240
Cash and cash equivalents	413
Bank overdrafts	(216)
Cash and cash equivalents in the cash flow statement	197

22. Restricted cash

Restricted cash at 31 March 2008 of £366 million consisted of deposits held as collateral in respect of loan note obligations within borrowings.

23. Deferred tax assets and liabilities

Recognised deferred tax assets and liabilities

Deferred tax is calculated in full on temporary differences under the liability method using the appropriate country tax rate. Deferred tax assets and liabilities have been offset where they relate to the same fiscal jurisdiction and when there is also a legally enforceable right to offset the associated current tax assets and liabilities. Deferred tax assets and liabilities are attributable to the following after offset:

	Net £million
Unrelieved tax losses	66
Accelerated capital allowances	(63)
Retirement benefit assets	(83)
Business combinations	(1,213)
Rolled over gains	(30)
Remittable earnings of associates and joint ventures	(69)
Other temporary differences	(87)
Net deferred tax assets/(liabilities)	**(1,479)**

Deferred tax is not provided on unremitted earnings of non-Sterling denominated subsidiaries except where the earnings are expected to be remitted in the foreseeable future, or where the Group does not control the timing of the remittance of such earnings.

The movement in the net deferred tax balance is as follows:

	£million
At beginning of period	–
Acquisition of Alliance Boots plc	(1,458)
Other acquisitions	(11)
Income statement credit	71
Charged to equity	(54)
Currency translation differences	(27)
At 31 March 2008	**(1,479)**

The movement in deferred tax assets and liabilities during the period is as follows:

	Unrelieved tax losses £million	Accelerated capital allowances £million	Retirement benefit assets £million	Business combinations £million	Rolled over gains £million	Remittable earnings of associates and joint ventures £million	Other temporary differences £million	Total £million
Deferred tax assets								
At beginning of period	–	–	–	–	–	–	–	–
Acquisition of Alliance Boots plc	53	–	–	–	–	–	–	53
Income statement credit	10	–	–	–	–	–	–	10
Currency translation differences	3	–	–	–	–	–	–	3
At 31 March 2008	**66**	–	–	–	–	–	–	**66**
Deferred tax liabilities								
At beginning of period	–	–	–	–	–	–	–	–
Acquisition of Alliance Boots plc	–	(50)	1	(1,259)	(32)	(54)	(117)	(1,511)
Other acquisitions	–	–	–	(11)	–	–	–	(11)
Income statement (charge)/credit	–	(12)	(28)	79	2	(5)	25	61
(Charged)/credited to equity	–	–	(56)	–	–	–	2	(54)
Currency translation differences	–	(1)	–	(22)	–	(10)	3	(30)
At 31 March 2008	–	**(63)**	**(83)**	**(1,213)**	**(30)**	**(69)**	**(87)**	**(1,545)**
Net deferred tax assets/(liabilities)								
At 31 March 2008	**66**	**(63)**	**(83)**	**(1,213)**	**(30)**	**(69)**	**(87)**	**(1,479)**

Unrecognised deferred tax assets and liabilities

The Group has only recognised a deferred tax asset on deductible temporary differences, unused tax losses or tax credits to the extent that future taxable profits will be available against which the asset can be utilised. The assets recorded are after reviewing the financial forecasts of the Group's position, depreciation and potential capital expenditure for capital allowances. Where it is not considered probable that a taxable profit will arise against which the temporary difference can be utilised, no asset has been recognised. Unprovided deferred tax on trading losses net of amortisation is £56 million and on capital losses is £nil. The trading losses have no expiry date.

The UK tax rate reduced from 30% to 28% on 1 April 2008. As this rate change was substantively enacted before the balance sheet date, it is reflected in the closing deferred tax balances and resulted in the release of a net deferred tax liability of £90 million.

24. Trade and other payables

	£million
Current	
Trade payables	1,849
Other taxation and social security	127
Accruals and deferred income	226
Other payables	307
	2,509

All amounts within current trade and other payables are due within one year.

	£million
Non-current	
Other payables	25
	25

25. Financial assets and liabilities

Outlined below is information regarding the contractual terms of the Group's borrowings. Further information on the Group's exposure to interest rate and currency risk is provided in note 26.

The carrying amount of financial assets and liabilities is as follows:

	£million
Current borrowings	
Bank overdrafts	(216)
Bank loans – other	(113)
Medium term notes	(14)
Loan notes	(368)
Finance lease liabilities	(22)
	(733)
Non current borrowings	
£300 million Eurobond 2009 5.5%	(300)
Bank loans – senior facilities	(7,503)
Bank loans – subordinated facility	(744)
Bank loans – other	(7)
Finance lease liabilities	(31)
	(8,585)
Total borrowings	(9,318)
Cash and cash equivalents	413
Total borrowings net of cash and cash equivalents	(8,905)
Restricted cash	366
Derivative financial instruments – currency and interest rate instrument assets	3
Derivative financial instruments – currency and interest rate instrument liabilities	(210)
Net borrowings	(8,746)
Available-for-sale investments	48
Trade payables	(1,849)
Trade receivables	1,780
Loans to customers	115
Net financial liabilities	(8,652)

The Group's principal net borrowings arise from the following sources:

1. A 10 year Eurobond of £300 million issued in 1999 carrying a fixed interest rate of 5.5% and held on the Group balance sheet at amortised cost.

2. £8,200 million of variable rate committed bank term loans. These loans, which are denominated in Sterling, Euros and Swiss Francs, are fully drawn and their carrying value at 31 March 2008 was £8,247 million including the impact of currency revaluation and reported net of unamortised fees incurred in respect of the loans. These loans mature between 2014 and 2017.

3. £368 million of loan notes classified within current borrowings, which can be redeemed by the holders giving notice prior to the semi-annual interest payment dates. If no such notice is given the notes will fall due on their contractual maturity dates which are between 2008 and 2014. The Group holds a floating rate interest bearing deposit of £366 million shown within restricted cash as collateral against loan notes with the same principal amount. This deposit is only available to the Group for the purpose of redeeming the associated loan notes.

The Group's bank overdrafts are repayable on demand.

Maturity profile of financial liabilities before the impact of derivative financial instruments

The table below shows the contractual maturities of financial liabilities on an undiscounted basis, including interest payments. Interest is calculated based on liabilities held at 31 March 2008 without taking account of any future debt issuance. Floating rate interest has been estimated using prevailing interest conditions at 31 March 2008. Cash flows in non-Sterling currencies are translated using exchange rates at 31 March 2008.

Terms and borrowings repayment schedule	Carrying value £million	Contractual cash flows £million	1 year or less £million	1-2 years £million	2-5 years £million	>5 years £million
Fixed						
£300 million Eurobond 2009 5.5%	(300)	(333)	(17)	(316)	–	–
Medium term notes	(4)	(4)	(4)	–	–	–
Finance lease liabilities	(53)	(82)	(26)	(14)	(16)	(26)
Floating						
Bank loans – senior facilities	(7,503)	(12,030)	(650)	(554)	(1,784)	(9,042)
Bank loans – subordinated facility	(744)	(1,714)	(68)	(59)	(204)	(1,383)
Loan notes	(368)	(377)	(377)	–	–	–
Bank loans – other	(120)	(120)	(113)	(4)	(2)	(1)
Bank overdrafts	(216)	(216)	(216)	–	–	–
Medium term notes	(10)	(10)	(10)	–	–	–
Total borrowings	(9,318)	(14,886)	(1,481)	(947)	(2,006)	(10,452)
Trade payables	(1,849)	(1,849)	(1,849)	–	–	–
Total non-derivative financial liabilities	(11,167)	(16,735)	(3,330)	(947)	(2,006)	(10,452)
Interest rate derivatives						
– outflows		(70)	(14)	(14)	(42)	–
– inflows		–	–	–	–	–
	(30)	(70)	(14)	(14)	(42)	–
Currency swaps						
– outflows		(614)	(129)	(20)	(465)	–
– inflows		400	97	17	286	–
	(179)	(214)	(32)	(3)	(179)	–
Currency exchange contracts						
– outflows		(364)	(364)	–	–	–
– inflows		363	363	–	–	–
	(1)	(1)	(1)	–	–	–
Total derivative financial liabilities	(210)	(285)	(47)	(17)	(221)	–
Total financial liabilities	(11,377)	(17,020)	(3,377)	(964)	(2,227)	(10,452)

All floating rate borrowings re-price within six months of the balance sheet date.

Currency profile

The analysis of financial assets and liabilities by currency (before the effect of currency hedging) is as follows:

	Total £million	Sterling £million	Euros £million	Swiss Francs £million	Other £million
Bank overdrafts	(216)	(79)	(120)	–	(17)
£300 million Eurobond 5.5%	(300)	(300)	–	–	–
Bank loans – senior facilities	(7,503)	(5,473)	(1,798)	(232)	–
Bank loans – subordinated facility	(744)	(744)	–	–	–
Bank loans – other	(120)	–	(89)	–	(31)
Medium term notes	(14)	–	–	–	(14)
Loan notes	(368)	(367)	(1)	–	–
Finance lease liabilities	(53)	(48)	(5)	–	–
Total borrowings	(9,318)	(7,011)	(2,013)	(232)	(62)
Cash and cash equivalents	413	273	102	–	38
Restricted cash	366	366	–	–	–
Available-for-sale investments	48	10	38	–	–
Trade payables	(1,849)	(882)	(767)	–	(200)
Trade receivables	1,780	734	899	–	147
Loans to customers	115	–	109	–	6
Derivative financial instruments – currency and interest rate instrument assets	3	3	–	–	–
Derivative financial instruments – currency and interest rate instrument liabilities	(210)	(210)	–	–	–
Net financial liabilities	(8,652)	(6,717)	(1,632)	(232)	(71)

25. Financial assets and liabilities (continued)

Finance lease liabilities

	Minimum lease payments £million	Interest £million	Principal £million
Less than one year	26	4	22
Between one year and five years	30	4	26
More than five years	26	21	5
	82	29	53

Under the terms of the lease agreements, no material contingent rents are payable.

Present value of minimum lease payments	£million
Less than one year	25
Between one year and five years	27
More than five years	17
	69

A comparison of carrying values and fair values of the Group's financial assets and liabilities held to finance the Group's operations as at 31 March 2008 is set out below:

	Carrying value £million	Fair value £million
Bank overdrafts	(216)	(216)
£300 million Eurobond 5.5%	(300)	(286)
Bank loans – senior facilities	(7,503)	(7,696)
Bank loans – subordinated facility	(744)	(768)
Bank loans – other	(120)	(120)
Medium term notes	(14)	(14)
Loan notes	(368)	(368)
Finance lease liabilities	(53)	(69)
Total borrowings	(9,318)	(9,537)
Cash and cash equivalents	413	413
Restricted cash	366	366
Derivative financial instruments		
– interest rate derivatives	(29)	(29)
– cross currency swaps	(178)	(178)
Net borrowings	(8,746)	(8,965)
Available-for-sale investments	48	48
Trade payables	(1,849)	(1,849)
Trade receivables	1,780	1,780
Loans to customers	115	115
Net financial liabilities	(8,652)	(8,871)

Fair values of bonds, available-for-sale investments and currency exchange contracts have been determined with reference to quoted market prices.

The fair values of interest rate derivatives and cross currency swaps have been calculated by discounting the future cash flows of the individual contracts using the appropriate market interest curve and currency exchange rate prevailing at 31 March 2008.

The fair value of bank overdrafts, bank loans – other, and loans to customers approximate to their carrying value due to either their short term nature or being re-priced at variable interest rates. The carrying values of the senior facilities and subordinated facility bank loans (which are variable rate) are lower than the fair values of the instruments due mainly to the impact of unamortised fees included in the carrying value.

All fair values are shown excluding any accrued interest (clean prices).

26. Financial instruments

Capital structure risk management

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital.

The ability of certain Group companies to pay dividends upwards, for ultimate distribution to shareholders, is restricted by the terms of the financing agreements to which they are party.

Liquidity risk management

Access to cost-effective funding is managed by maintaining a range of committed and uncommitted facilities, sufficient to meet anticipated needs, arranging funding ahead of requirements, and developing diversified sources of funding.

Group liquidity is optimised through cash pooling and deposits with or loans from Group treasury companies.

The Group's core borrowing is provided through £8,200 million of committed term loans which are fully drawn. The carrying value of these loans, which are denominated in Sterling, Euros and Swiss Francs, at 31 March 2008 was £8,247 million including the impact of currency revaluation and reported net of unamortised fees incurred in respect of the loans. These loans mature between 2014 and 2017. The Group also has access to a committed £820 million revolving credit facility, £200 million of which has been utilised in providing a guarantee to the Boots Pension Scheme and £620 million of which was available as at 31 March 2008. This facility provides access to funding in a range of currencies and is available until 2014.

The Group's net borrowings vary throughout the year in a predictable seasonal pattern. In particular, net borrowings peaks in the period September to December due to the working capital requirements of Christmas trading.

The Group monitors its net debt position on a daily basis against both budget and a rolling two month cash forecast. The maturity profile of the Group's financial liabilities at 31 March 2008 are shown in note 25.

Credit risk

The maximum exposure to credit risk is represented by the carrying amount of each financial asset, including derivative financial instruments, at the balance sheet date.

Credit risk exposure to commercial counterparties is managed through credit control functions in each of the businesses. New customers are credit checked, customer limits are reviewed at least annually and aged debtor reviews are undertaken regularly.

The Group considers the possibility of significant loss in the event of non-performance by a financial or commercial counterparty to be unlikely.

The ageing of trade receivables and customer loans at 31 March 2008 was:

	£million
Not past due	**1,701**
Past due < 3 months	**148**
Past due 3–6 months	**15**
Past due 6–12 months	**21**
Past due more than one year	**10**
Total trade receivables and customer loans	**1,895**

At 31 March 2008 there were no significant concentrations of credit risk in respect of trade creditors and customer loans. The most significant such credit exposure of the Group at 31 March 2008 was to the National Health Service in the UK.

The maximum exposure to credit risk for trade receivables and customer loans at 31 March 2008 by geographic region was:

	£million
UK	**733**
Other European countries	**1,155**
Other countries	**7**
Total trade receivables and customer loans	**1,895**

Exposures to financial counterparties arise from the use of derivative financial instruments, cash balances and short term deposits. The Group protects itself against the risk of financial loss arising from the failure of financial counterparties by setting ratings based limits to the maximum exposure to individual counterparties or their groups. Limits are set by reference to ratings issued by the major rating agencies, Standard and Poor's and Moody's Investors Service Limited.

At 31 March 2008 total exposures of the Group to financial counterparties was £782 million of which £3 million related to derivative financial assets, £413 million in respect of cash and cash equivalents, and £366 million in respect of restricted cash.

£605 million of derivative financial assets, cash and cash equivalents and restricted cash relate to balances managed centrally by Group treasury spread across a number of high quality counterparties, all of whom have a credit rating of A or better. The remaining £177 million of cash and cash equivalents represents short term deposits, cash-in-transit and cash held in operational bank accounts across the Group. An analysis of the Group's cash and cash equivalents is provided in note 21.

26. Financial instruments (continued)

Market risk

Market risk is the risk that changes in market prices, such as currency exchange rates and interest rates will affect the Group's income or the value of its holdings of financial instruments. The objective of market risk management is to manage market risks within acceptable parameters. The Group transacts in financial instruments including derivatives in order to manage these risks in accordance with the Group treasury policies approved by the Board.

Currency risk

The Group is party to a variety of currency derivatives in the management of exchange rate exposures, including cross currency swaps and currency exchange contracts. Movements in the fair value of all forward exchange contracts other than those designated and effective as cash flow hedges or net investment hedges are reported directly in the income statement.

Currency transaction risk

The Group utilises forward exchange derivatives to hedge significant committed and highly probable future transactions and cash flows.

At 31 March 2008, the Group had outstanding forward currency exchange contracts with a notional principal of £7 million that are designated and effective as cash flow hedges of committed and highly probable future transactions. Fair value movements of these contracts are deferred in equity until the hedged transaction takes place. These contracts all mature within one year of the balance sheet date.

A £1 million gain has been deferred in equity as at 31 March 2008 in respect of these contracts, which is expected to be recycled through the income statement within one year of the balance sheet date. A loss of £1 million has been transferred to the income statement in respect of contracts designated as cash flow hedges that have matured during the period to 31 March 2008.

The Group has significant non-Sterling denominated currency net investments denominated in Euros and Swiss Francs. The Group uses derivative financial instruments, specifically cross currency swaps, forward currency exchange contracts and non-Sterling currency borrowings to hedge the non-Sterling currency risk.

The Group has a number of cross currency swap contracts in place. At 31 March 2008, the fair value of the Group's cross currency swaps is a liability of £178 million. £14 million of the liability relates to currency swaps designated as net investment hedges of non-Sterling denominated currency net investments. Movements in fair value are deferred in equity until the underlying hedged investment is sold. The remaining liability of £164 million relates to currency swaps designated as held for trading. The currency exchange risk associated with these swaps is hedged through the use of short dated forward currency exchange contracts designated as held for trading. At 31 March 2008 the fair value of these offsetting currency exchange contracts was a £1 million liability.

The effect of currency swaps and forward contracts to manage translation risk on net borrowings is shown below:

	Before hedging £million	After hedging £million
Sterling	(6,579)	(6,473)
Euro	(1,911)	(1,928)
Swiss Franc	(232)	(289)
Other	(24)	(56)
Total net borrowings	(8,746)	(8,746)

At 31 March 2008 the total notional amount of outstanding currency exchange contracts that the Group has committed was £758 million.

At 31 March 2008 the balance sheet carrying value of the Group's outstanding forward exchange contracts was a £1 million asset and a £1 million liability.

Currency risk – sensitivity analysis

The table below shows the Group's sensitivity to non-Sterling exchange rates on its non-Sterling financial instruments excluding trade payables and trade receivables, which do not represent a significant exposure to exchange rates.

A 10% strengthening of Sterling against the following currencies at 31 March 2008 would have increased/(decreased) equity and profit by the amounts shown below. This analysis assumes that all other variables, including interest rates, remain constant and that instruments designated as net investment hedges at 31 March 2008 remain highly effective. In this table financial instruments are only considered sensitive for exchange rates where they are not in the functional currency of the entity that holds them.

	Impact on equity £million	Impact on profit £million
Euro	75	3
Swiss Franc	29	1
Other	2	(4)

A 10% weakening of Sterling against these currencies at 31 March 2008 would have had the equal and opposite effect to that shown above on the basis that all other variables remain constant.

The movements in equity relate to non-Sterling borrowings and currency swaps used to hedge Group assets denominated in those currencies. An appreciation in the value of the borrowing or currency swap would be matched by a corresponding depreciation in the value of the Group asset which would also be in equity. Exchange rate sensitivities on Group assets other than financial instruments are not shown in the table above.

Interest rate risk

The Board's policy is to protect its ability to service its debt obligations by ensuring that floating rate interest payments on not less than 50% of the principal outstanding under the facilities raised to finance the acquisition of Alliance Boots plc are hedged. Exposures are hedged through a combination of interest rate caps and interest rate swaps.

The Group has a mixture of fixed and floating rate borrowings. Before the impact of derivative financial instruments, £357 million (4%) of borrowings are at fixed interest rates (predominantly relating to the £300 million Eurobond 2009 5.5%). The re-pricing risk of the fixed borrowings coincides with their maturity. The floating rate borrowings re-price within 6 months of the reporting date, based on short term borrowing rates for the relevant currency.

The Group has interest rate swaps with a notional principal of £500 million to swap £500 million of outstanding borrowings from floating to fixed interest rates. The Group also has purchased interest rate caps with notional principal amounts of £3,500 million and €1,600 million respectively to protect the Group from rising interest rates on the corresponding amount of borrowings. In the period to 31 March 2008 no amounts were deferred in equity in respect of these instruments. All of the fair value movements in these instruments from inception to 31 March 2008 have been recognised in the income statement.

After taking into account the impact of derivative financial instruments, £5,611 million (60%) of the Group's total borrowings are at fixed or capped interest rates. All other borrowings re-price within six months of the reporting date.

At 31 March 2008 £5,258 million (64%) of the principal outstanding under the facilities raised to finance the acquisition of Alliance Boots plc was hedged.

The impact of a 1% increase and a 1% decrease in interest rates on 31 March 2008 on pre-tax profit are shown in the table below. This analysis assumes that all other variables had been constant throughout the period. On this basis there would have been no significant amounts recognised directly in equity.

	1% increase in interest rates £million	1% decrease in interest rates £million
Gain/(loss) – derivative financial instruments	**89**	**(42)**
(Loss)/gain – variable rate financial instruments	**(66)**	**66**

Derivative financial instruments

Achieving hedge accounting is based on measuring the effectiveness of the derivative as a hedging instrument as well as fulfilling hedge documentation rules. The effectiveness test compares the change in the fair value of the designated derivative and the change in the fair value of the hedged item, to determine if this ratio falls within the permitted range of 80% to 125%. Any derivative that falls outside the permitted range is classified as held for trading. Gains or losses on the derivative are recognised immediately in the income statement except where the derivative is designated within an effective cash flow or net investment hedge relationship, in which case the gains and losses are deferred in equity and are recycled through the income statement at the time that the hedged item is recognised in the income statement. The hedge accounting treatment is described further in the accounting policies.

Where a derivative does fall within the permitted range but is not 100% effective, the ineffective element is recognised in the income statement immediately. This gives rise to a gain or loss which is recognised under Finance income or Finance costs as appropriate. These gains or losses represent timing differences that will reverse over the life of the financial instruments.

27. Analysis of movement in net borrowings

Set out below is a reconciliation of the net increase in cash and cash equivalents to the increase in net borrowings at 31 March 2008. Net borrowings are defined by the Group as borrowings net of cash and cash equivalents, restricted cash, and derivative financial instruments.

	£million
Net increase in cash and cash equivalents	**210**
Increase in restricted cash	**366**
Cash and cash equivalents inflow from increase in debt and debt financing	**(7,317)**
Movement in net borrowings resulting from cash flows	**(6,741)**
Loan notes issued for non-cash consideration	**(366)**
Borrowings acquired with businesses	**(1,247)**
Finance leases entered into	**(10)**
Amortisation of prepaid financing fees	**(27)**
Capitalised finance costs	**(19)**
Currency translation differences and fair value adjustments on financial instruments	**(336)**
Movement in net borrowings in the period	**(8,746)**
Net borrowings at beginning of period	**–**
Net borrowings at 31 March 2008	**(8,746)**

27. Analysis of movement in net borrowings (continued)

Set out below is an analysis of the movement in net borrowings during the period:

	Cash and cash equivalents £million	Restricted cash £million	Borrowings within current liabilities £million	Borrowings within non-current liabilities £million	Derivative financial instruments £million	Net borrowings £million
At beginning of period	–	–	–	–	–	–
Net increase in cash and cash equivalents	413	–	(203)	–	–	210
Increase in restricted cash	–	366	–	–	–	366
Cash and cash equivalents inflow from increase in debt and debt financing	–	–	(134)	(7,183)	–	(7,317)
Loan notes issued for non-cash consideration	–	–	–	(366)	–	(366)
Borrowings acquired with businesses	–	–	(383)	(732)	(132)	(1,247)
Finance leases entered into	–	–	–	(10)	–	(10)
Amortisation of prepaid financing fees	–	–	–	(27)	–	(27)
Capitalised finance costs	–	–	–	(19)	–	(19)
Currency translation differences and fair value adjustments on financial instruments	–	–	(13)	(248)	(75)	(336)
At 31 March 2008	413	366	(733)	(8,585)	(207)	(8,746)

In the Group cash flow statement, cash and cash equivalents include bank overdrafts which are classified as borrowings within current liabilities in the balance sheet which amounted to £216 million at 31 March 2008.

28. Movement in borrowings on acquisitions, disposals and investments in associates and joint ventures

	£million
Acquisition of businesses – cash	(10,790)
Acquisition of businesses – loan notes issued for non-cash consideration	(366)
Cash and cash equivalents net of overdrafts of businesses acquired	420
Disposal of businesses	20
Purchase of investments in associates and joint ventures	(41)
Borrowings acquired with businesses	(1,247)
	(12,004)

Of the total movement in borrowings on acquisitions, disposals and investments in associates and joint ventures, £11,886 million relates to the acquisition of Alliance Boots plc, and £118 million relates to other acquisitions.

29. Provisions

	Refurbishment and reorganisation £million	Vacant property £million	Closure or termination of operations £million	Other £million	Total £million
At beginning of period	–	–	–	–	–
Acquisition of Alliance Boots plc	74	12	24	5	115
Provisions created during the period	–	8	2	2	12
Provisions utilised during the period	(25)	(4)	(3)	–	(32)
Provisions released during the period	–	–	(6)	(1)	(7)
At 31 March 2008	49	16	17	6	88
Current	8	5	14	4	31
Non-current	41	11	3	2	57
	49	16	17	6	88

Refurbishment and reorganisation

The refurbishment and reorganisation provision relates primarily to store refurbishments and supply chain reorganisation in the UK business within the Health & Beauty Division. The majority of these costs are expected to be incurred in the next two years. In respect of the store refurbishment programme estimates of expected costs have been based on a store-by-store survey and comprise management's view of lease obligations.

Vacant property

The vacant property provisions represent recognition of the present value of the expected net costs arising from vacant properties and sub-let properties. The exact timing of utilisation of these provisions will vary according to the individual properties concerned.

Closure or termination of operations

The provision for closure or termination of operations relates mainly to restructuring of Contract Manufacturing, supply chain configuration, costs associated with restructuring contractual arrangements with third-party IT providers and the balance of the provision for an onerous supply contract following the disposal of Boots Healthcare International in 2006. The majority of the costs are expected to be incurred within the next year.

30. Capital and reserves

Reconciliation of movement in capital and reserves	Share capital £million	Share premium £million	Retained earnings £million	Other reserves £million	Shareholders' equity £million	Minority interests £million	Total equity £million
At beginning of period	–	–	–	–	–	–	–
Issue of share capital	1,005	2,795	–	–	3,800	–	3,800
Acquisition of Alliance Boots plc	–	–	–	–	–	16	16
Total recognised income and expense for the period	–	–	137	76	213	2	215
Contribution from minority interests	–	–	–	–	–	17	17
At 31 March 2008	1,005	2,795	137	76	4,013	35	4,048

Other reserves
Other reserves comprise:

Translation reserve
The translation reserve comprises all currency exchange differences arising from the translation of the financial statements of non-Sterling denominated operations that are not integral to the operations of the Company, as well as from the translation of liabilities that hedge the Company's net investment in non-Sterling denominated subsidiaries. The balance of the translation reserve at 31 March 2008 was a £99 million credit.

Hedging reserve
The hedging reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions that have not yet occurred. The balance of the hedging reserve at 31 March 2008 was a £1 million credit.

Available-for-sale reserve
The available-for-sale reserve includes the cumulative net change in the fair value of available-for-sale investments, until the investment is derecognised. The balance of the available-for-sale reserve at 31 March 2008 was a £24 million debit.

31. Share capital

	Number of shares	£million
Ordinary shares of 1,000 CHF:		
Authorised	2,000,000	1,005
Allotted, called up and fully paid	2,000,000	1,005

32. Operating leases
The operating lease rental expense in the period was:

	£million
Land and buildings	229
Other	11
	240

At 31 March 2008 the Group had outstanding commitments for future minimum lease payments under non-cancellable operating leases which fall due as follows:

	£million
Less than one year	270
Between one and five years	929
More than five years	1,297
	2,496

The Group leases a large number of its properties under operating leases. The leases run predominantly for periods from 1 to 25 years, with options to renew the leases at the end of the period. Lease rentals are increased in regular intervals to reflect market rentals. None of the leases include material contingent rentals.

Rental income from subleased properties was £12 million.

33. Commitments and contingent liabilities
Commitments
Future capital expenditure approved by the Directors and not provided for in these Consolidated Financial Statements at 31 March 2008 was £34 million.

Contingent liabilities
The Group has no material contingent liabilities other than those arising in the normal course of business.

34. Pensions

The Group operates a number of pension schemes in the UK and other countries including both defined benefit and defined contribution schemes.

The principal scheme is the Boots Pension Scheme. This scheme, which is closed to new members, has continued with its investment strategy of planning to hold 15% of assets in equity and property to back long term liabilities, and 85% of assets in a diverse portfolio of high quality bonds to match liabilities up to 35 years. The other large scheme is the Alliance UniChem UK Group Pension Scheme. This scheme, which is also closed to new members, plans to hold 50% of funds in return seeking assets such as equities and 50% in investments with cash flows which match projected pension obligations under a liability driven investment strategy. Both schemes have entered into Memoranda of Understanding with the Group. This resulted in the payment of £102 million of additional contributions during the period, an agreement that conservative investment strategies would be maintained and that a further £366 million of contributions will be made over ten years from August 2008, of which £20 million will be paid in 2008/09 and each of the following four financial years.

Amounts recognised in the balance sheet	**£million**
Present value of defined benefit obligation	**(3,584)**
Fair value of pension scheme assets	
– bonds	**3,140**
– equities	**496**
– other plan assets	**245**
	3,881
Retirement benefit	
– assets	**317**
– liabilities	**(20)**
	297

Changes in the present value of the defined benefit obligation	**£million**
At beginning of period	**–**
Acquisition of Alliance Boots plc	**3,696**
Current service cost	**43**
Past service cost	**2**
Interest on pension scheme liabilities	**157**
Employee contributions	**18**
Actuarial gains and losses	**(228)**
Benefits paid	**(113)**
Currency translation differences	**9**
At 31 March 2008	**3,584**

Changes in the fair value of pension scheme assets	**£million**
At beginning of period	**–**
Acquisition of Alliance Boots plc	**3,693**
Contributions	**160**
Employee contributions	**18**
Expected return on pension scheme assets	**163**
Actuarial gains and losses	**(47)**
Benefits paid	**(113)**
Currency translation differences	**7**
At 31 March 2008	**3,881**

The Group expects to contribute around £90 million, including £20 million of deficit funding, to its defined benefit pension schemes in the year ended 31 March 2009.

The expense recognised in the income statement is as follows:

	£million
Current service cost	**(43)**
Past service cost	**(2)**
	(45)
Expected return on pension scheme assets	**163**
Interest on pension scheme liabilities	**(157)**
	(39)

The expense is recognised in the following line items in the income statement:

	£million
Profit from operations	(45)
Finance income	163
Finance costs	(157)
	(39)

The amounts recognised in the statement of recognised income and expense are as follows:

	£million
Experience gains on pension scheme liabilities	3
Changes in assumptions underlying the present value of pension scheme liabilities	225
Experience losses on pension scheme assets	(47)
	181
Cumulative amount of actuarial gains and losses recognised in the statement of recognised income and expense	181

Principal actuarial assumptions at the balance sheet date	UK	Non-UK
Discount rate for pension scheme liabilities	6.8%	5.8%
Inflation	3.6%	2.2%
Rate of general long term increase in salaries	5.1%	2.6%
Rate of increase to pensions in payment	3.5%	1.6%

Expected return on pension scheme assets	UK
Bonds	5.8%
Equities	8.1%
Property	7.1%
Other net assets	5.4%

The expected return on plan assets of non-UK pension plans was 5.0% to 6.4%. The expected rate of return on pension scheme assets has been determined with reference to market returns at the balance sheet date. The actual return on pension scheme assets was £116 million.

The mortality assumption used to value the majority of scheme liabilities is based on 2000 series tables, with scaling factors of 110% for males and 120% for females, allowing for medium cohort improvements. This has been adjusted to take account of the actual experience of schemes where this data is of sufficient size. The impact of medium cohort improvements has been included recognising the continued recent improvements in published mortality investigation data. The mortality assumptions will continue to be reviewed to ensure they remain appropriate.

Projected life expectancy from age 60	Currently aged 45	Currently aged 60
Male	26.7	25.7
Female	28.3	27.4

A sensitivity analysis on the principal assumptions used to measure the scheme liabilities is as follows:

	Change in assumption	Impact on scheme liabilities
Discount rate	Increase by 0.25%	Decrease by 4.1%
Rate of inflation	Increase by 0.25%	Increase by 4.0%

An increase of one year in the assumed life expectancy at age 60 would increase the defined benefit obligation by 2.5%.

Amounts for the current period	£million
Defined benefit obligation	(3,584)
Pension scheme assets	3,881
Retirement benefit assets	297
Experience adjustments on pension scheme liabilities	3
Experience adjustments on pension scheme assets	(47)

Defined contribution schemes

The Group operates a number of defined contribution pension arrangements. During the period the Group contributed £10 million.

35. Related parties

Parent and ultimate controlling party

At 31 March 2008 AB Acquisitions Holdings Limited was the immediate and ultimate parent company of Alliance Boots GmbH.

AB Acquisitions Holdings Limited is incorporated in Gibraltar, and its registered office is 57/63 Line Wall Road, Gibraltar. AB Acquisitions Holdings Limited is jointly controlled by certain funds advised by Kohlberg Kravis Roberts & Co. L.P. and Alliance Santé Participations S.A., a company indirectly wholly owned by S. Pessina. S. Pessina and O. Barra, who are Directors of Alliance Boots GmbH, are also directors of Alliance Santé Participations S.A.

Key management personnel

Key management personnel comprise the Directors of Alliance Boots GmbH and, in addition, W. Zettel through his directorship of AB Acquisitions Holdings Limited. The Directors of Alliance Boots GmbH are:

S. Pessina* (Executive Chairman)
O. Barra*
S.W.J. Duncan*
G.R. Fairweather*
M. Pagni*
D. Murphy
M. Caprioli
S. D'Angelo
C. Britton
A. De Nunzio
E. Jornod
N.C.E. Land

* executive Directors

Key management personnel remuneration

The remuneration of the key management personnel of the Group during the period comprised:

	£million
Short term employee benefits	**3**
Post-employment benefits	–

Other transactions with key management personnel

On the acquisition of Alliance Boots plc, shareholders, including key management personnel, were able to elect to receive consideration in the form of loan notes. The amount of loan notes owing to key management personnel at 31 March 2008 was £0.2 million including principal and interest. The loan notes, which accrue interest at commercial rates, can be redeemed by giving notice prior to the semi-annual interest payment dates, and if no such notice is given the notes will fall due on their contractual maturity dates which are between 2008 and 2014.

Together with other senior managers, the executive Directors were invited to participate in a management equity plan which is designed to enable them, as investors, to share in the future financial success of the Group through an investment of personal capital. To assist participation, the Group offered loans under commercial terms, and at 31 March 2008 the loan amounts outstanding in respect of key management personnel was £0.6 million. The loans are repayable in annual instalments over five years to June 2012.

Key management personnel may purchase goods for personal and family use from the Health & Beauty Division business in the UK, on the same terms and conditions as those available to all other UK employees of the Group.

Transactions with other related parties

As disclosed in the shareholder circular sent to the shareholders of Alliance Boots plc on 8 May 2007, Kohlberg Kravis Roberts & Co. L.P. and Alliance Santé Participations S.A. (or their respective designees) were each entitled to fees on completion of the acquisition of Alliance Boots plc. As a result, fees of £53.9 million and £52.9 million respectively were paid after the acquisition was completed.

As disclosed in the shareholder circular, Kohlberg Kravis Roberts & Co. L.P. and Alliance Santé Participations S.A. (or their respective designees) are each entitled to receive an annual monitoring fee. During the period, each party received £1.8 million, of which £0.6 million and £1.8 million was outstanding at 31 March 2008 respectively.

During the period, S. Pessina acquired a beneficial interest in £10 million of the principal of the £300 million Eurobond 2009 5.5%, originally issued by a subsidiary of Alliance Boots plc. The bond was issued in May 1999, is due for repayment in 2009, and is publicly traded.

The Group paid £0.1 million for accounting services to an entity which is considered to be a related party by virtue of it being jointly controlled by a director of AB Acquisition Holdings Limited. The transaction was on an arm's length basis.

The Group, in its normal course of business, transacts with other entities controlled or significantly influenced by Kohlberg Kravis Roberts & Co. L.P.. All transactions are carried out on an arm's length basis.

Subsidiary undertakings

The principal subsidiary undertakings, all of which were indirectly held, were:

	Percentage held by subsidiary undertakings	Country of operation	Country of incorporation	Main activity
Health & Beauty Division				
Boots UK Limited	100	UK	England and Wales	Pharmacy-led health and beauty retailing
Alliance UniChem Norge A.S.	100	Norway	Norway	Pharmacy-led health and beauty retailing
Boots Retail (Ireland) Limited	100	Eire	Eire	Pharmacy-led health and beauty retailing
Alliance Apotheek B.V.	100	The Netherlands	The Netherlands	Retail pharmacy operator
Boots Retail (Thailand) Limited	100	Thailand	Thailand	Pharmacy-led health and beauty retailing
Pharmaceutical Wholesale Division				
Alliance Healthcare France S.A.	99.8	France	France	Pharmaceutical wholesaling
UniChem Limited	100	UK	England and Wales	Pharmaceutical wholesaling
Alliance Healthcare S.A.	99.2	Spain	Spain	Pharmaceutical wholesaling
Alleanza Healthcare Italia SpA	100	Italy	Italy	Pharmaceutical wholesaling
Alliance Healthcare B.V.	100	The Netherlands	The Netherlands	Pharmaceutical wholesaling
Alliance Healthcare s.r.o.	97.1	Czech Republic	Czech Republic	Pharmaceutical wholesaling
Apteka Holding ZAO	66	Russia	Russia	Pharmaceutical wholesaling
Holtung A.S.	100	Norway	Norway	Pharmaceutical wholesaling
Boots Beauty International Limited	100	UK	England and Wales	Wholesaling of Boots branded products
Contract Manufacturing				
BCM Limited	100	UK	England and Wales	Manufacturing

In addition to the direct holding in Apteka Holding ZAO above, Hedef Alliance Holding A.S., an associate in which the Group has a 50% interest, has a direct interest of 30% in Apteka Holding ZAO.

Associates and joint ventures

The Group's principal associates and joint ventures were:

	Percentage interest in ordinary share capital and voting rights	Country of operation	Country of incorporation	Main activity
Associates				
Hedef Alliance Holding A.S.	50	Turkey	Turkey	Pharmaceutical wholesaling
Andreae-Noris Zahn AG	29.99	Germany	Germany	Pharmaceutical wholesaling
Galenica A.G.	25.5	Switzerland	Switzerland	Pharmaceutical manufacturing, wholesaling and retailing
Alliance Healthcare S.A.	49	Portugal	Portugal	Pharmaceutical wholesaling
Joint venture				
Guangzhou Pharmaceutical Corporation	50	China	China	Pharmaceutical wholesaling

Transactions with associated undertakings and joint ventures, all of which are carried out on an arm's length basis were:

	£million
Revenue in period	**4**
Purchases in period	**(1)**
Amounts due from	**1**
Amounts due to	**(1)**

During the period the Group disposed of its prewholesale and contracts logistics business in Portugal to Alliance Healthcare S.A., the Group's Portuguese associate, for £5 million.

36. Accounting estimates and judgements

In preparing the Consolidated Financial Statements, the management of Alliance Boots GmbH are required to make estimates and judgements. The matters described below are considered to be the most important in understanding the judgements that are involved in preparing these statements and the uncertainties that could impact the amounts reported in the results of operations, financial position and cash flows. The Group accounting policies are described in note 2.

Fair value measurement on a business combination

The measurement of fair values on a business combination requires the recognition and measurement of the identifiable assets, liabilities and contingent liabilities. The key judgements involved are the identification and valuation of intangible assets which involves estimation of future cash flows and the selection of a suitable discount rate.

Impairment of indefinite life intangible assets (including goodwill)

The Group has significant carrying values of goodwill and intangible assets, such as pharmacy licences, brands and customer relationships following the acquisition of Alliance Boots plc. Goodwill and other indefinite life intangibles, such as pharmacy licences, and certain brands are held at cost and tested annually for impairment. Amortised intangible and tangible assets are tested for impairment where events show an indication of impairment. The impairment test involves estimation of future cash flows and the selection of a suitable discount rate. This requires an estimation of the value in use of the cash generating units to which the intangible assets are allocated (see note 15).

Measurement of defined benefit pension obligations

The Group accounts for pension costs relating to retirement plans in accordance with IAS 19 'Employee Benefits'. In applying IAS 19, the pension costs are assessed in accordance with the advice of independent qualified actuaries. This requires the exercise of significant judgements in relation to the estimation of future changes in salaries and inflation, as well as mortality rates, the expected return on assets and the selection of a suitable discount rate. Further detail is provided in note 34.

Revenue

In the Health & Beauty division, reimbursement of dispensing revenue is initially estimated because the actual reimbursement is often not known until after the month of sale.

In respect of loyalty schemes (principally the Boots Advantage Card), a liability is recorded to estimate the proportion of the points issued which will be redeemed by customers.

Supplier rebates

The recognition of supplier rebates can require estimation when the reporting period end is not coterminous with the end of the predetermined period over which the rebate is earned.

Provisions

Provisions are recognised in the period when it becomes probable that there will be a future outflow of funds resulting from past operations or events which can be reasonably estimated. The timing of recognition requires the application of judgement to existing facts and circumstances, which can be subject to change.

Estimates of the amounts of provisions recognised are based on current legal and constructive requirements, technology and price levels. Actual outflows can differ from estimates due to changes in laws, regulations, public expectations, technology, prices and conditions, and can take place many years in the future, and therefore the carrying amounts of provisions are regularly reviewed and adjusted to take account of such changes.

37. Risk assessment

The Group's executive Directors play the leading role in internal controls, monitoring the overall risk profile and regularly reporting to the Board through the audit committee. In addition, the Board through the executive Directors is responsible for determining clear policies as to what the Group considers to be acceptable levels of risk. These policies seek to enable people throughout the Group to use their expertise to identify risks that could undermine performance and to devise ways of bringing them within acceptable levels. Where risks are identified that are not acceptable, action plans are developed to mitigate them with clear allocation of responsibilities and timescales for completion and ensure that progress towards implementing these plans is monitored and reported upon.

Further detail on the risks faced by the Group and the internal control process are set out in the Annual Review.

Glossary of key terms

Exceptional items
Items classified by Alliance Boots GmbH as exceptional in nature. These are not regarded as forming part of the trading activities of the Group and so merit separate presentation to allow stakeholders to understand the elements of financial performance and assess trends in financial performance. In 2007/08 these mainly comprised costs in relation to merger synergies, systems rationalisation and supply chain reconfiguration projects, and costs in relation to the acquisition of Alliance Boots plc.

Net borrowings
Cash and cash equivalents, restricted cash, derivative financial instruments and borrowings net of unamortised prepaid financing fees.

Trading profit
Profit from operations before exceptional items, amortisation of customer relationships and brands, and share of post tax earnings of associates and joint ventures.

Alliance Boots GmbH

All rights reserved

© Copyright 2008 Alliance UniChem IP Limited

Designed and produced by Addison Corporate Marketing (London).

Alliance Boots GmbH
Baarerstrasse 78
CH-6300 Zug
Switzerland

Contact
enquiries@allianceboots.com